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288-984—66——1

In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 642

BALTIMORE AND OHIO RAILROAD COMPANY, ET AL., APPELLANTS

v.

UNITED STATES OF AMERICA, ET AL.

No. 680

THE DELAWARE AND HUDSON RAILROAD CORPORATION, APPELLANT

v.

UNITED STATES OF AMERICA, ET AL.

No. 691

ERIE-LACKAWANNA RAILROAD COMPANY, APPELLANT

v.

UNITED STATES OF AMERICA, ET AL.

ON APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

MEMORANDUM FOR THE UNITED STATES

STATEMENT

On October 4, 1966, a three-judge federal district court in the Southern District of New York denied

requests to enjoin an order of the Interstate Commerce Commission approving the immediate consummation of a merger between the Pennsylvania Railroad Company and the New York Central Railroad Company. On October 18, this Court stayed the Commission's order pending disposition of the appeals from the district court's decision, and, in the same order, announced an expedited schedule for the filing, briefing, and oral argument of the appeals. Eight railroads have perfected appeals—the Baltimore and Ohio and Chesapeake and Ohio railroads, their affiliates, and the Norfolk and Western Railway Company, in No. 642; the Delaware and Hudson Railroad Corporation in No. 680; and the Erie-Lackawanna Railroad Company in No. 691.[1]

The controversy involves all the principal railroads in the northeastern United States. The merger applicants—the Pennsylvania and the New York Central—are the first and third largest rail systems in the region. They are concentrated in the midwestern and Middle Atlantic States. There are two other major

[1] There were several other complaining parties in the district court proceeding. A number of communities in New Jersey and Pennsylvania, and Milton J. Shapp, a resident of Pennsylvania and stockholder of the Pennsylvania Railroad Company, filed applications in this Court to stay the Commission's order, but they have not yet perfected appeals by filing jurisdictional statements. Accordingly, it would be premature to comment on the issues which they may raise. One of the railroad complainants below, Boston and Maine, has not appealed. It has stated that it is satisfied that the Commission will protect its interests adequately.

systems. The first comprises the Chesapeake and Ohio, the Baltimore and Ohio, and their affiliates (C&O–B&O).[2] The second is the Norfolk and Western (which, since 1964, owns or controls the Nickel Plate and the Wabash). Both systems are generally parallel to, though somewhat more southward oriented than, either Penn or Central. There are also several smaller roads not affiliated with one of the four major systems. The largest of these is the Erie-Lackawanna. It extends from New York City to Chicago and serves a number of points in New York, New Jersey, Pennsylvania and Ohio. The others are the Boston and Maine Corporation and The New York, New Haven and Hartford Railroad Company, in New England, and The Delaware and Hudson, which operates mainly in New York State.[3]

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[2] Chesapeake and Ohio and Baltimore and Ohio are under common ownership. See *Chesapeake & O. Ry. Co.—Control—Baltimore & O.R. Co.*, 317 I.C.C. 261, sustained *sub nom. Brotherhood of Maintenance of Way Employees* v. *United States*, 221 F. Supp. 19 (E.D. Mich.), affirmed *per curiam*, 375 U.S. 216.

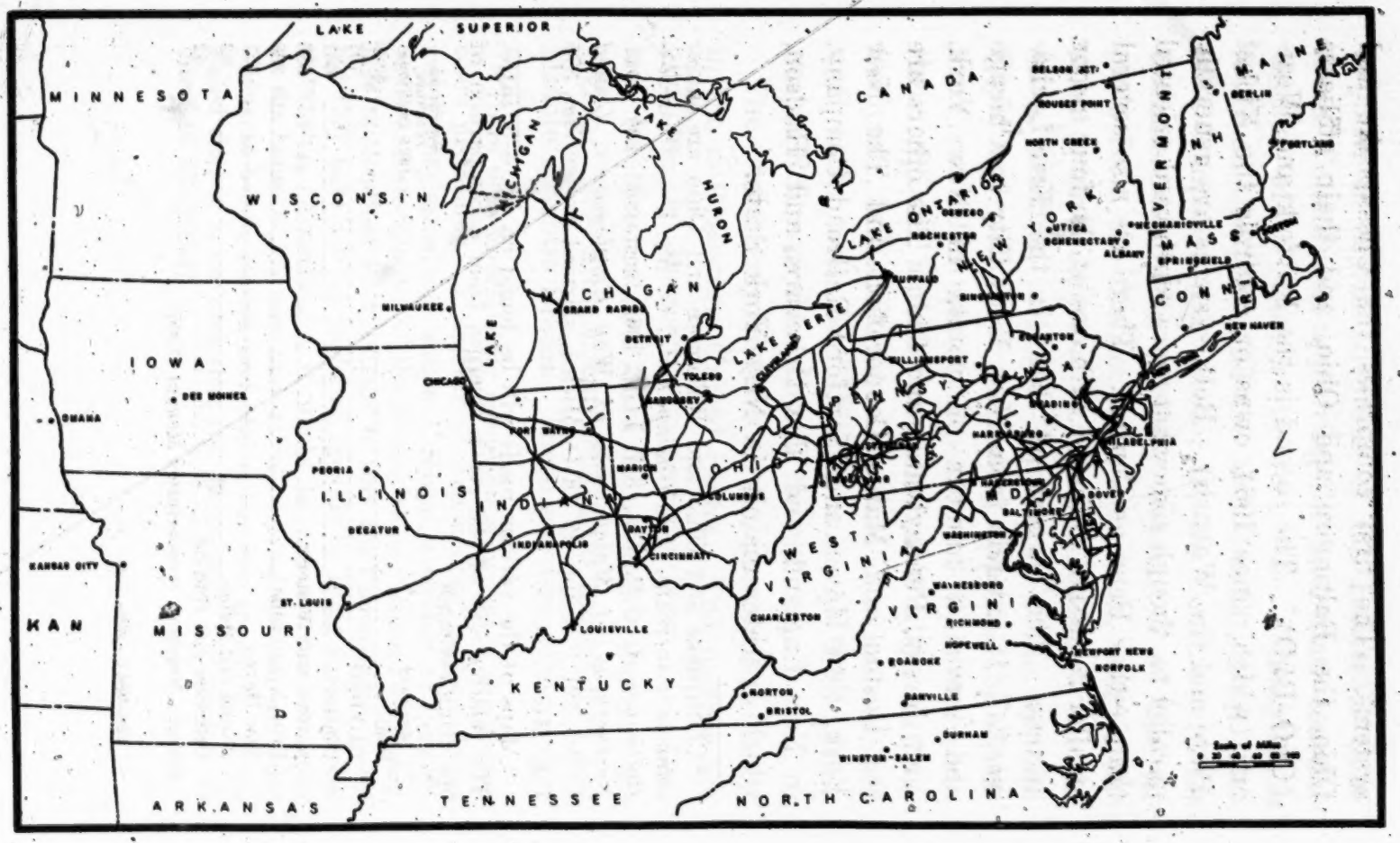
[3] Maps of the various roads will be found on pp. 4–8, *infra*. The relative size of the roads emerges from a comparison of operating revenues:

Railroad	Operating revenues, 1965 (millions)
Penn	$893
C&O-B&O	797
Central	661
Norfolk and Western	592
Erie-Lackawanna	230
New Haven	121
Boston and Maine	63
Delaware and Hudson	42

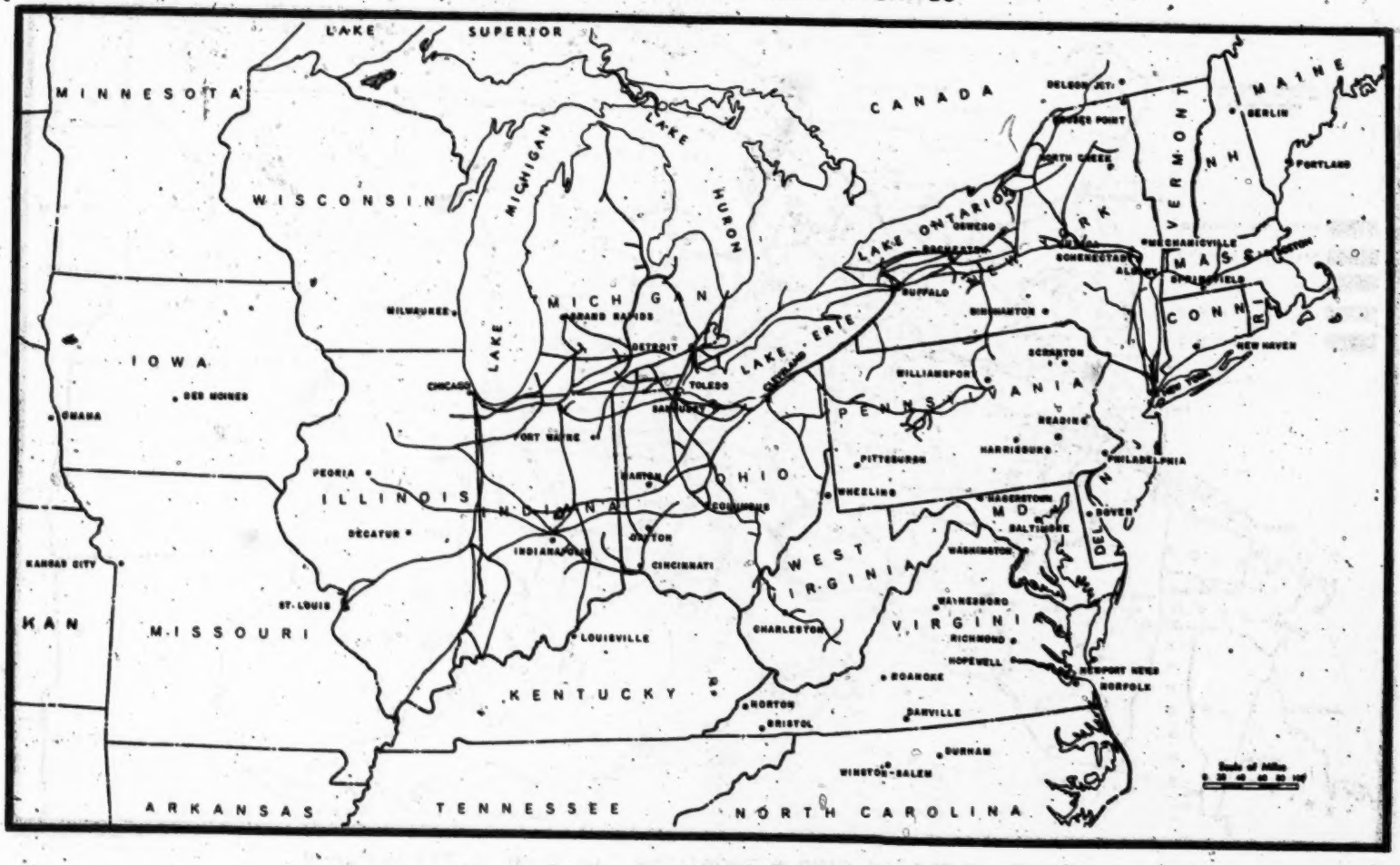
Source: *Moody's Transportation Manual* (1966).

238-984 O—66——2

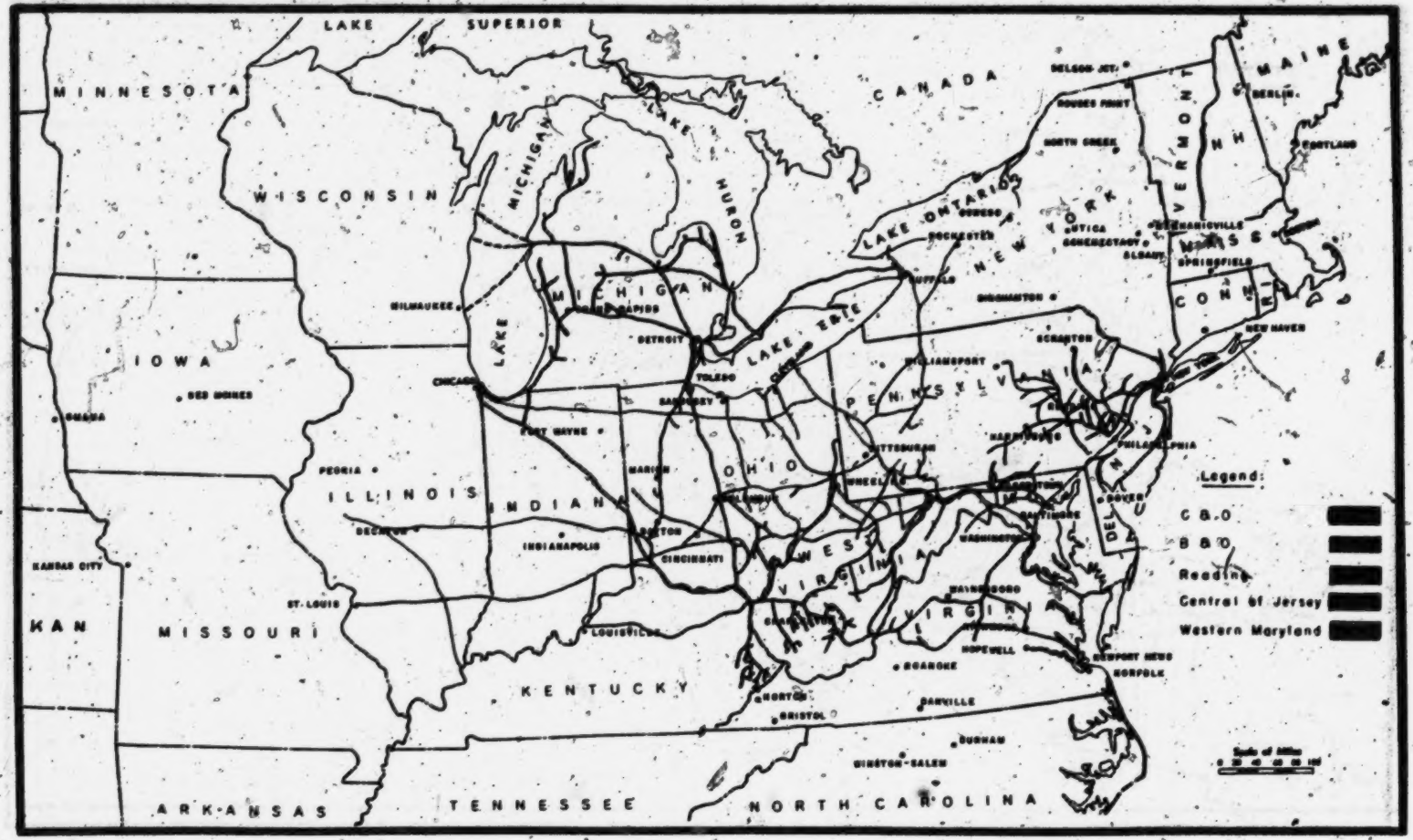
PENNSYLVANIA R.R. AND AFFILIATES



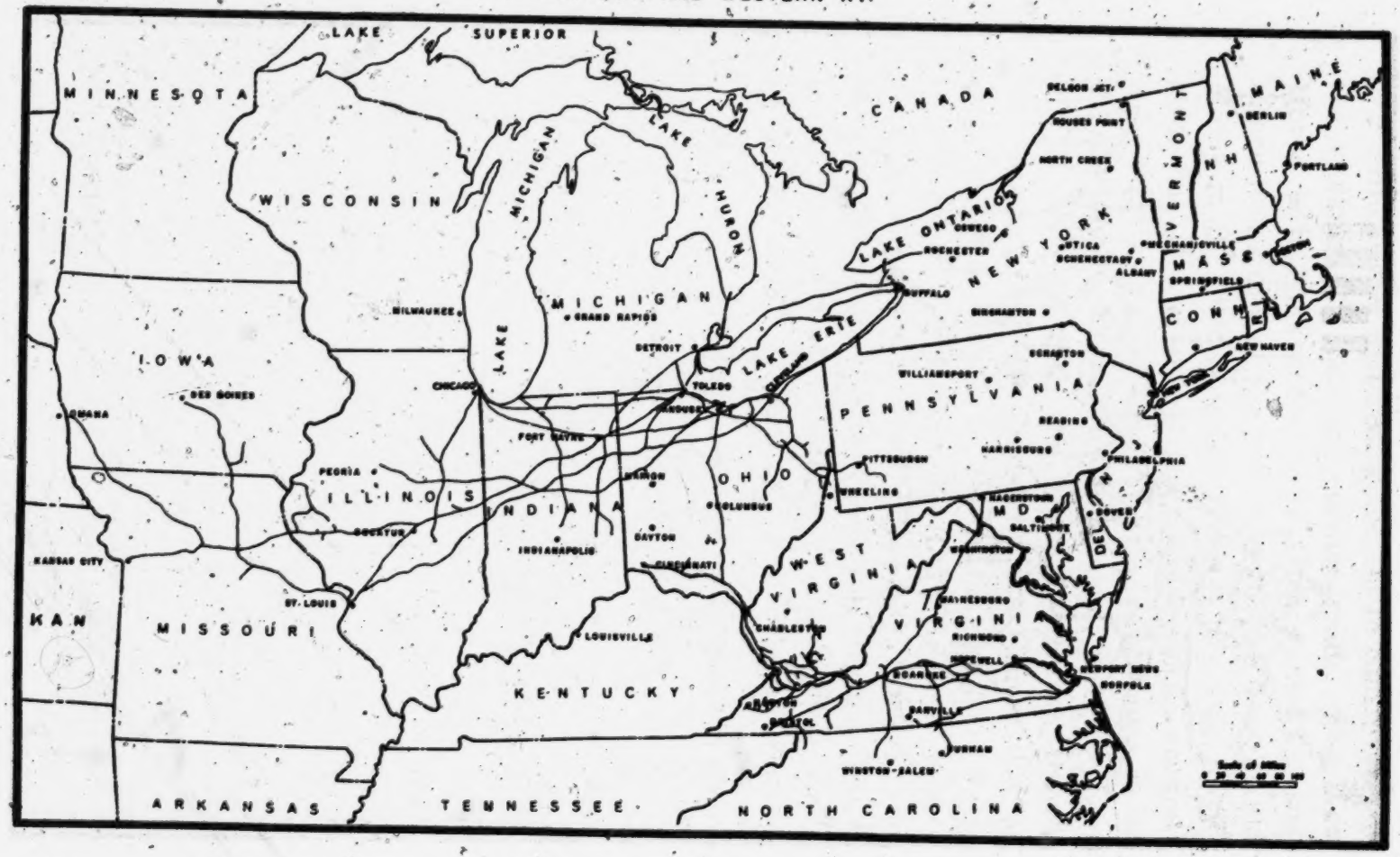
NEW YORK CENTRAL RY. AND AFFILIATES



CHESAPEAKE & OHIO RY., BALTIMORE & OHIO RY., AND AFFILIATES



NORFOLK AND WESTERN RY.



EASTERN DISTRICT RAILROADS NOT AFFILIATED WITH MAJOR SYSTEMS

A critical fact underlying the entire controversy is the weakness of the four smaller roads. The New Haven is in bankruptcy. Erie-Lackawanna has sustained losses in 7 of the last 10 years and Boston and Maine in 8. Delaware and Hudson has been profitable, but its revenues—never great—have declined considerably in this period.[4] Erie-Lackawanna is by far the largest of these roads and, aside from the New Haven, the one with the bleakest earnings record. Its situation was considered by the Commission at some length in *Norfolk & W. Ry. Co. and New York, C. & St. L. R. Co. Merger*, 324 I.C.C. 1, 19–29, a proceeding involving the merger of the Norfolk and Western and Nickel Plate roads and the acquisition by the merged roads of control of the Wabash Railroad Company.[5] Originally, the Erie-Lackawanna

[4] The gross revenues and net income of Erie-Lackawanna, Boston and Maine, and Delaware and Hudson, over the past decade, have been as follows (*Moody's Transportation Manual* (1966)):

Year	E-L		B & M		D & H	
	Operating Revenues	Net Income	Operating Revenues	Net Income	Operating Revenues	Net Income
1956	175.9	8.2	88.0	0.7	57.4	9.1
1957	173.2	3.6	86.0	0.8	55.8	7.6
1958	152.7	−3.7	77.4	−2.4	46.5	3.3
1959	154.3	−5.7	72.0	−3.8	46.2	5.4
1960	165.1	−14.4	67.8	−3.8	43.3	5.7
1961	*211.0	−26.5	66.0	−3.3	41.1	1.8
1962	210.9	−16.6	64.0	−2.9	41.3	2.8
1963	206.0	−17.1	63.6	−2.9	41.1	3.1
1964	212.4	−8.3	61.9	−5.2	41.7	4.4
1965	230.0	3.3	63.2	−0.6	42.0	5.0

*Delaware, Lackawanna & Western R.R. Co. operations were combined with Erie's upon merger of the companies on October 17, 1960.

[5] It was this unification proceeding that propelled Norfolk and Western into the ranks of the major eastern systems.

had asked that the Commission require its inclusion in the Norfolk and Western system as a condition to approving the merger.[6] In the course of the proceeding, however, it withdrew its request on the basis of an agreement with Norfolk and Western under which it was to receive financial assistance from that road pending negotiations looking toward eventual inclusion. The parties believed that Erie-Lackawanna's "financial straits" constituted "an insurmountable obstacle in the negotiation of reasonable terms at this time" and that affiliation would have to "be deferred until Erie-Lackawanna can substantially improve its earnings position." 324 I.C.C. 1, 21.

The Commission, while noting certain beneficial results that affiliation between the roads might produce, declined to override the parties' judgment and require immediate inclusion. It found Erie-Lackawanna's "financial condition * * * such as to render it impossible to frame terms for its inclusion which would be, as required by statute, fair, equitable, or reasonable" from the standpoint of either road (*id.* at 22). It emphasized not only Erie-Lackawanna's "precarious financial plight" but also "the burden another railroad would assume if it absorbed the Erie-Lackawanna now" (*id.* at 25). However, the Com-

[6] The Commission has no authority to compel railroad mergers. But all unification proposals must be submitted to the Commission for its approval (Interstate Commerce Act, § 5(2), 49 U.S.C. 5(2)), and in passing upon them the Commission is expressly empowered to impose "such terms and conditions * * * as it shall find to be just and reasonable" (Section 5(2)(b)), such as inclusion of a road that would be injured by the proposal.

mission did provide, as a condition of its approval of the Norfolk and Western-Nickel Plate merger, that it would entertain a petition for inclusion in the Norfolk and Western system filed by Erie-Lackawanna within five years (p. 28), and it made the same provision for the Delaware and Hudson and the Boston and Maine (p. 32). This ruling was made in June 1964; it forms an essential backdrop to the issues raised in these appeals.

The application of Penn and Central for permission to merge was filed with the Commission in 1962. Lengthy administrative proceedings ensued, and it was not until April 6, 1966, that the Commission rendered its final decision, approving the merger subject to certain conditions. *Pennsylvania R. Co.—Merger—New York Central R. Co.*, 327 I.C.C. 475. In the meantime the Erie-Lackawanna, Delaware and Hudson, and Boston and Maine had filed, in September 1965, petitions for inclusion in the Norfolk and Western, and a few weeks later the Norfolk and Western and C&O–B&O had filed an application to merge with each other and had coupled their proposal with a qualified offer to include the three smaller roads in the merged system.

However, neither the inclusion proceeding nor the merger proceeding was completed when the Commission rendered its decision in the Penn-Central case,[7] and the uncertainty of their destiny in the emerging pattern of the northeastern railroad structure naturally caused acute concern to the three smaller

[7] Nor are they yet (see p. 17, *infra*.)

roads.[8] In the Penn-Central proceeding, they alleged that the merger would inflict serious competitive injury on them and argued that either consummation of the Penn-Central merger should be postponed until their future was finally determined or, alternatively, that they should be included in Penn-Central. The Commission accepted the premise of this argument, stating:

> The service the three petitioners render their shippers is essential and the public interest dictates that it be preserved. Unless somehow protected, through inclusion herein or by some other equitable means, the petitioners would be adversely affected by the proposed merger to a serious degree and would be severely handicapped in providing required transportation to the highly industrialized areas they serve. [327 I.C.C. at 529; see, also, pp. 531–532.]

It declined, however, to order their inclusion in Penn-Central, to consolidate the Penn-Central proceeding with the inclusion proceeding, or to postpone consummation of the Penn-Central merger until their future was determined.

The Commission chose to withhold action on the three roads' request for inclusion in Penn-Central until the Norfolk and Western inclusion proceeding

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[8] The fourth, the New Haven, is to be included in the Penn-Central system under terms still to be worked out. It is not an appellant. However, the application of a group of New Haven bondholders to enjoin the Penn-Central merger until the New Haven is actually included, or at least until interim protective conditions for it are imposed, is now pending in the court below (see, also, p. 20, n. 15, *infra*).

was completed (which might, of course, moot the request), and, during the interim period pending inclusion of the three roads in some major system, to impose stringent conditions for the protection of the traffic and revenues of the three roads against the anticipated adverse impact of the Penn-Central merger. Emphasizing the volume of traffic that might be diverted from the already weak smaller roads by Penn-Central, the Commission deemed it "doubtful that, without inclusion in a major system, these three carriers could withstand the competition of the applicants merged," and held that "unless they are protected during the period necessary to determine their future, we would not authorize consummation at this time, even though approving the merger." 327 I.C.C. at 532. Accordingly, it made its approval subject to acceptance by the merger applicants of specified conditions for the protection of the three roads from "impairment or serious weakening" resulting from the merger (*ibid.*). The conditions (pp. 561–563) were of two types: traffic conditions requiring Penn-Central to maintain existing practices and route patterns with respect to traffic for which the protected roads compete; and financial, or "indemnity", conditions guaranteeing the protected roads a fixed share of the combined total of Penn-Central's and their revenues, so as to protect them against loss of income should any of their traffic be diverted to Penn-Central.

The Commission's disposition of the problem of the protected roads was, however, unsatisfactory both to them and to two of their major competitors (C&O–

B&O and Norfolk and Western, the "non-protected" roads), and proceedings to set aside the Commission's order of April 6 approving the merger were instituted in the district court by both groups [9]—which also filed petitions for reconsideration with the Commission advancing the same contentions as before the district court. The protected roads argued that the conditions were ambiguous in many particulars and inadequate, and that indemnification for any impairment of their capital that the merger might cause should also be required. They asked the Commission to order consummation of the merger postponed, at least until fully certain and sufficient conditions were imposed, preferably until their inclusion in one of the major systems was finally determined. The non-protected roads, on the other hand, argued that, as competitors of the protected roads, they would be seriously harmed by the indemnity conditions that the Commission had prescribed. These conditions, they contended, gave the protected roads a direct interest in Penn-Central's revenues and hence, they argued, an incentive to divert to Penn-Central traffic which they would normally route over the lines of the non-protected roads.

In a brief urging reconsideration by the Commission, the United States agreed that the indemnity conditions raised serious questions and that, since they had been adopted without any hearing or notice to the parties, the appropriate course would be to reopen

[9] There were other plaintiffs as well, who challenged the Commission's approval of the merger on broader grounds. See p. 2, n. 1, *supra*.

the proceeding for a fuller consideration of the question, meanwhile postponing consummation of the merger. We suggested an additional reason for delay—the need to assess the impact of the merger on C&O–B&O and Norfolk and Western in the light of certain recent developments.

The hearing examiners had found that the Penn-Central merger would "not be detrimental" to the remaining major systems in the Northeast (Examiners' Report, p. 305). They had based this finding solely on the failure of C&O–B&O or Norfolk and Western to introduce any evidence on the point (*id.*, pp. 301–305). The Commission in its opinion likewise assumed there would be no adverse effect on these roads. However, in its petition for reconsideration, C&O–B&O claimed that, in fact, the merger would have a substantial adverse impact on it. Moreover, in the recently instituted C&O–B&O–Norfolk and Western merger proceeding and in the Norfolk and Western inclusion proceeding, both C&O–B&O and Norfolk and Western argued that the Penn-Central merger would upset the competitive balance in the Northeast and that this prospect gave persuasive support to *their* merger application, especially if inclusion of the protected roads in Norfolk and Western was the Commission's preferred solution to the problem of those roads. C&O–B&O primarily sought from the Commission assurance that its failure to present evidence of competitive injury in the Penn-Central proceeding would not estop it to present such evidence in the other proceedings; we urged that the Penn-Central

proceeding should be reopened to receive such evidence.

On September 16, 1966, the Commission issued its report on reconsideration. It declined to delay consummation of the merger, in part because it believed that delay might force the New Haven into liquidation. It did, however, find sufficient merit in the challenges to the indemnity conditions to rescind them pending a hearing on whether they should be modified to avoid harm to the non-protected roads and whether a capital-loss indemnification condition should be added.[10] In thus permitting the merger to be consummated without the indemnity conditions, the Commission did not modify or refer to the finding in its original opinion that the conditions prescribed there were essential and that without them it would not permit the merger to be consummated.

When the Commission's report on reconsideration was issued, the protected and the non-protected roads urged with renewed vigor in the district court proceeding that an injunction against the Commission's order approving immediate consummation of the merger should be granted. Both groups argued that the Commission's action in permitting the merger to go forward before the fate of the protected roads had been settled was improper. The protected roads expressed fear of irreparable injury in the period when they would be denied inclusion in a major system—and

[10] The Commission also declined to reopen the proceeding for the further purpose of receiving evidence concerning injury to C&O–B&O, while ruling that C&O–B&O was not estopped to offer such evidence in its merger proceeding.

hence compelled to compete as independents against Penn-Central—without the protection of the full set of conditions orginally imposed by the Commission to keep them afloat while their future was worked out. The non-protected roads argued that the Commission had committed itself to imposing stringent conditions that would harm them.

In form, the request was for a preliminary injunction. The district court treated it as such and, applying the criteria of *Virginia Petroleum Jobbers Ass'n* v. *Federal Power Commission*, 259 F. 2d 921 (C.A. D.C.), denied the request by a divided vote, Judge Weinfeld dissenting.[11] The same day (October 4), the Commission denied a request by the C&O–B&O and Norfolk and Western to expedite their merger proceeding, and postponed the commencement of hearings in that proceeding until further order of the Commission.[12] On October 31, 1966, hearings in the reopened proceeding on the indemnity conditions commenced; they have not, as of this writing, been fully completed (see p. 31, n. 24, *infra*). Hearings in the proceeding on the petitions of Erie-Lackawanna, Delaware and Hudson, and Boston and Maine for inclusion in the Norfolk and Western system were completed in August 1966; the examiners'

[11] The United States was a statutory defendant in the district court proceeding (see 28 U.S.C. 2322) but neither supported nor opposed the granting of a preliminary injunction. In view of our position below, and not being an appellant, we refrain from injecting issues not presented by the appeals.

[12] We have printed the order of October 4 as an Appendix to this memorandum. Pp. 33–37, *infra*.

report is awaited. Consummation of the Penn-Central merger remains stayed, of course, as a result of the order of this Court.

DISCUSSION

At the outset, we emphasize the scope of the decision below. First, the district court declined to preserve the *status quo* pending plenary judicial review of the merits of the Commission's order approving the merger of the Penn and Central. That, we think, was erroneous,[12] but not, so far as the present appeals are concerned, crucial. More pertinently, for present

[12] No one questions that the district court's decision now under review must realistically be viewed as finally determining the merits of the Commission's action approving the merger. Indeed, actual consummation of a railroad merger of this character and magnitude, after Commission approval and under leave of court, inevitably prejudices the ultimate outcome of the judicial review proceedings. Doubtless the principle operates in some degree for every large merger. But it has special force with respect to a railroad consolidation which involves the re-arrangement and elimination of important physical facilities. A court which has permitted the integration of two large railroad systems would ordinarily be most reluctant to order them unravelled.

It follows that consummation should have been stayed, in any event, until the court had given itself an opportunity to consider the matter on the merits—at least in the absence of very compelling considerations requiring immediate consolidation. There was no such urgency here. As the court itself recognized, so slight a delay would not have seriously prejudiced the fate of the New Haven. Nor was there a colorable claim that the survival of the merging roads would be endangered if they did not integrate immediately. The court's only expressed concern was that the improvements in service expected from the merger would be delayed if consummation were postponed. Whatever the merits of that prediction in light of the severe traffic conditions imposed for the interim period, we doubt that

purposes, by refusing to enjoin consummation of the merger until the Commission had resolved serious problems created by the consolidation the court gave irrevocable [14] assent to a procedure which we are constrained to question quite independently of any concern for fuller review of the merger's merits.

We stress two respects in which the administrative procedure approved by the district court was truncated. In the first place, although expressly noticing the acute problems that the merger would create for three lesser roads whose prayers for inclusion in one or another major rail system were before it, the Commission permitted immediate integration of Penn and Central without deciding the ultimate fate of those injured companies. Secondly, consummation was authorized before interim protective con-

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it outweighed the interest in assuring full consideration of this major merger.

In this context, we are tempted to read the court's action as a deliberate ruling on the merits. Yet, considering the summary nature of the judicial proceedings and the apparently uncritical application of traditional temporary-injunction tests, it is difficult to say that the court treated the matter on the merits. On this ground alone, it is arguable that the case should be remanded to the district court for the entry of a stay pending judicial review. We do not, however, urge that disposition. No issue of the merits of the merger is raised by the present appeals, and, as we explain below (pp. 30–32), the procedural issue they do raise can best be dealt with, in our judgment, by a somewhat different course.

[14] Insofar as the court refused to delay consummation of the merger until the Commission had considered and resolved questions relating to the fate of the other affected roads, its decision is, in every sense, final. Once the merger is consummated, any contention that the Commission granted permission to consummate prematurely is, obviously, moot.

ditions for the benefit of those smaller roads—and others,[15] notably the New Haven—had been finally settled.

In our view, the court's acquiescence in this manner of proceeding presents a serious question: Where a major railroad merger is bound to create serious problems for other roads, may the Commission permit immediate consummation before solving those problems? Such a merger permanently alters the structure of the railroad industry in the region.[16] It thereby creates a new and different framework in which the problems of the affected roads must be solved. Yet, those problems may not admit of a satisfactory solution under the changed conditions resulting from the merger. When that possibility cannot be ruled out, it would seem that the problems of the other roads should be solved before, not after, the merger is allowed to go forward.

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[15] The Commission left for future settlement the terms on which the New Haven will be included in Penn-Central, and a group of New Haven bondholders has applied to the court below to enjoin the merger until the New Haven is actually included in the Penn-Central or, at the least, until conditions for the protection of the New Haven in the interim are imposed on Penn-Central (see p. 12, n. 8, *supra*). Reading and Central of New Jersey (affiliates of C&O–B&O) also contend that the Commission's action in permitting immediate consummation of the Penn-Central merger leaves them without necessary protection.

[16] This assumes that (1) the merger is indeed a major one and (2) extensive physical consolidation and integration of facilities is contemplated that would render the merger, as a practical matter, irreversible once consummated. The Penn-Central merger meets both conditions.

So saying, we do not suggest that the Commission must devise, or can require adherence to, a "master plan" for railroad unifications in each region.[17] Nor is it our contention that every loose end must be neatly tied up before a merger application is approved (see 49 U.S.C. 5(9)). The Commission undoubtedly enjoys great flexibility in these matters. But we question whether it can properly permit the irrevocable step of consummation when vexing problems involving the merger's impact on other important railroads remain unresolved, merely on the hope that their resolution on terms consistent with the public interest is feasible and will not be unduly delayed. Such a course, as we shall presently explain, seems difficult to reconcile with the Commission's statutory obligation to approve only those railroad mergers "consistent with the public interest" (49 U.S.C. 5(2)(b)), and to administer all provisions of the Interstate Commerce Act so as to promote a sound transportation system (National Transportation Policy, 49 U.S.C. preceding § 1).

Finally, we emphasize that, in questioning the Commission's procedure, we do not quarrel with the merits of the Penn-Central merger proposal itself. Indeed, the agencies of the Executive Branch that have substantive responsibilities for the formulation of economic and transportation policy believe that the merger is in the public interest and that its consummation should be promptly effected. They point

[17] See *St. Joe Paper Co.* v. *Atlantic Coast Line R. Co.*, 347 U.S. 298, 305. Compare Transportation Act, 1920, 41 Stat. 481.

out that the railroad industry of the Northeast is in urgent need of rapid modernization and believe that, as a practical matter, substantial consolidation among existing systems will be necessary to achieve this end. While recognizing that, in theory, it might be possible to devise a better alignment than that which the Penn-Central merger will produce, they stress that the Commission has no power under existing law to compel consolidations. The real choice, in the opinion of these agencies, is between Penn-Central and the existing four-system structure; and they regard the former as preferable from the standpoint of the public interest in a sound, efficient, and modern rail transportation industry.

This view expressly assumes, however, that a place in the emerging pattern of consolidation in the Northeast can be found for the lesser roads of the region. Indeed, an important reason why consolidation is supported is that it may provide a solution to the serious financial condition of these roads. Thus, while not contesting the Commission's action in approving the Penn-Central merger in principle, we deem it necessary to advert to the question whether the Commission's procedure—under which consummation of the merger is to precede the completion of the proceedings to determine the place of the lesser roads—may endanger the prospects for a successful resolution of the problem of those roads.

We begin with a fact that none disputes. The three railroads that will feel the impact of the Penn-

Central merger most keenly—Erie-Lackawanna, Delaware and Hudson, and Boston and Maine—constitute a vital segment of the railroad industry of the Northeast. Unwanted orphans they may be, owing to their financial weakness and vulnerability, but, with aggregate operating revenues of $335 million (1965) (see p. 3, n. 3, *supra*), they cannot be considered negligible factors in the regional structure. The Commission expressly found that the service they render their shippers is "essential" (327 I.C.C. at 529), and that finding has not been challenged.

Nor is there substantial question that the Penn-Central merger threatens the very survival of these smaller roads; that, to withstand the competition of the Penn-Central system, they must eventually be absorbed into a major system like Norfolk and Western; and that, in the meantime, they must be protected against competitive inroads by Penn-Central.[18] It is against this background that the Commission's efforts to deal with the problems that the merger creates for the three affected roads, without delaying the consummation of the merger, must be appraised.

CONDITIONS

In approving the merger, the Commission, in its order of April 6, 1966, prescribed extensive conditions—described by the district court as unprecedented in their severity—for the protection of the three roads while their future was being worked out. These

[18] These were the findings of the Commission in its original opinion (Statement, *supra*, pp. 12–13); it has never receded from them.

conditions would have prohibited Penn-Central from actively attempting to capture the traffic of the other roads and also purported to guarantee the protected roads an adequate level of revenue in the event that the traffic conditions failed to prevent substantial diversion. The severity of the conditions and the Commission's insistence that the merger applicants accept them without litigation suggest that the consummation of the merger might indeed place those roads in a rather critical position.

On reconsideration, however, the Commission rescinded the revenue conditions pending a hearing upon them. We do not quarrel with the Commission's action in so doing. The conditions were novel; they had been adopted without any hearing or notice to the parties; and there was a serious question whether they might not cause undue injury to the unprotected roads. We are concerned, however, with the soundness of the Commission's decision not to require a delay in the consummation of the merger until the final conditions could be worked out.

In its April 6 opinion the Commission said that without consent by the merger applicants to the conditions it was prescribing for the protection of Erie-Lackawanna, Delaware and Hudson, and Boston and Maine, it would not permit the merger to be consummated. But in its order of September 16, without a reference to its earlier statement, it cut back the conditions substantially while at the same time authorizing immediate consummation. It is perhaps debatable whether the indemnity conditions were truly essential in light of the traffic conditions or

whether their withdrawal will in fact place the protected roads in imminent jeopardy. But in a matter of this gravity it is dangerous to try to read between the lines and supply reasons—however plausible—that the Commission itself failed to articulate. Having initially found that immediate consummation of the merger would not be in the public interest unless certain conditions were in force, the Commission should not, we believe, have reversed itself without explanation.

It is idle to speculate on the considerations that led the Commission to alter its view. Agency action cannot be sustained on grounds that the agency does not express. *United States* v. *Chicago, M., St. P. & P. R. Co.*, 294 U.S. 499, 511; *Securities and Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80, 94. In addition, there is reason to doubt that the Commission had completely adequate grounds here. To be sure, it expressed fear that any delay in the consummation of the merger would imperil the New Haven's chances of staving off liquidation. But the district court itself declared that the resolution of the New Haven's uncertain status lacked the urgency that the Commission ascribed to it. As for the other benefits the merger is thought likely to produce, it is agreed that they will, of necessity, be realized only over a long period of time. It may be questioned whether hastening the process justifies the danger of impairing the viability of the affected roads.

The Commission may also have felt that the conditions controversy could be resolved promptly, before irreparable injury would come to the protected roads.

That is doubtless why it ordered hearings to commence on October 31, 1966. However, the non-protected roads appear intransigently opposed to any form of indemnity conditions, and the protected roads forcefully assert that they require not only revenue indemnification but capital indemnification. They express fear that the Penn-Central system will regard a temporary obligation to guarantee the protected roads an adequate revenue as but a small price to pay for destroying their capital value and resources, and thereby precluding their absorbtion into a major system on reasonable terms. These fears cannot be dismissed out of hand as completely groundless. And Penn and Central have reserved the right to contest, in the courts if necessary, any capital-indemnity condition the Commission might impose.

Our hope is that the Commission will soon resolve the disputes and devise conditions that are both effective and fair (see p. 31 and n. 24, *infra*). Certainly the Commission has the power and the recognized obligation to hammer out a solution. But the difficulties are sufficiently formidable to create an appreciable danger that the final resolution of the matter will come too late to save the protected roads if meanwhile they face the competition of Penn-Central without the full protective conditions that the Commission said were essential.

INCLUSION

Even if adequate protective conditions are imposed and take effect before the intended beneficiaries are irreparably harmed, the problem of the survival of the protected roads in the face of the Penn-Central

combination will not be solved, but only postponed. Whatever their final form, the conditions will only be temporary. To restrain Penn-Central permanently from making any changes in its existing practices or routes that might harm Erie-Lackawanna, Delaware and Hudson, or Boston and Maine would preclude the system from achieving many of the economies that are the principal justification for the merger. To give the three smaller roads a permanent stake in the financial success of Penn-Central would be almost like decreeing their affiliation with the Penn-Central system and thereby giving that system a virtual rail monopoly in New England and New York—probably not a very satisfactory solution to the problem of the protected roads.[19]

The conditions, in short, are designed for interim relief only. Under no view do they resolve the ultimate destinies of the protected roads. It has long been assumed that eventually these roads must be absorbed in one or another of the major systems. The Commission itself assumes that the Penn-Central merger makes such a solution unavoidable (p. 23, n. 18, *supra;* Statement, *supra,* pp. 12–13). However, by permitting that merger to be consummated before deciding where the protected roads can best be absorbed, we fear lest the Commission may have impaired its ability to achieve a workable solution in the public interest.

In the Norfolk and Western-Nickel Plate merger proceeding (see Statement, *supra,* pp. 9–10), the

[19] In Map 1 at the end of this memorandum, we show the pattern that would result if the three protected roads, as well as the New Haven, were part of the Penn-Central system.

Commission observed that Erie-Lackawanna probably belonged in the expanded Norfolk and Western system created by that merger.[20] But the Commission declined to require its inclusion as a condition of approving the merger, in view of Erie-Lackawanna's financial weakness and the burden to Norfolk and Western if it were required to absorb Erie-Lackawanna in that state. It did, however, grant Erie-Lackawanna, along with Delaware and Hudson and Boston and Maine, the right to petition within five years for inclusion in Norfolk and Western. That right has been exercised and the inclusion proceeding is nearly completed.

Norfolk and Western there argues that it is no more capable now than it was in 1964 of absorbing Erie-Lackawanna and the other roads, especially since Erie-Lackawanna's financial picture has not noticeably brightened.[21] Emphasizing the alleged competitive pressures it will face from Penn-Central when that merger is consummated, Norfolk and Western claims that it can absorb the three weak roads only if its application to merge with C&O–B&O—also now pending before the Commission—is granted. These contentions cannot at this stage be deemed wholly insubstantial. Should they turn out to be well

[20] In Map 2, we show the alignment contemplated there.

[21] For the first time in a number of years, Erie-Lackawanna in 1965 showed a modest profit (see Statement, *supra*, p. 9, n. 4). Norfolk and Western contends, however, that Erie-Lackawanna's overall financial state and prospects remain very poor. We have lodged with the Court the briefs filed by Norfolk and Western in the inclusion proceeding, setting forth its contentions.

founded, the Commission might find that, by permitting the Penn-Central merger to be consummated before deciding upon the future of the protected roads, it has been drawn into approving the proposed Norfolk and Western–C&O–B&O merger as well.

The Commission has never indicated that it would consider such a merger consistent with the public interest. Indeed, in its order declining to accelerate the hearing of the merger application, the Commission intimated considerable doubt on that score.[22] The propriety of such a merger has been questioned [23] and Penn and Central are opposed. Yet, if Norfolk and Western is correct in contending that it cannot, in the face of Penn-Central, absorb the protected roads with their grave problems unless it is united with C&O–B&O, may not the Commission be compelled, however reluctantly, to approve the merger simply in order to save the protected roads? The only remaining alternative at that stage would be to include the protected roads in Penn-

[22] It stated: [B]oth applicants herein * * * have consummated other major railroad unifications within the past four years, without providing any indication that they contemplated or required any further unifications in the foreseeable future" (*Norfolk and Western Ry. Co.—Merger, Etc.—Chesapeake and O. Ry. Co.*, Finance Docket No. 23832, Order of October 4, 1966, p. 2; Appendix, *infra*, p. 36).

[23] A merger of C&O–B&O and Norfolk and Western would create a virtual monopoly of the very important traffic in coal between the border States and the Norfolk port area, whence it is exported abroad. See Map 3 at the end of this memorandum.

Central, and the monopolistic character of that solution (see p. 27, *supra*) makes it a questionable course.

Nor need we assume that the competitive impact of Penn-Central on Norfolk and Western will be as great as Norfolk and Western contends; it may simply be that the protected roads are still too weak to be included on reasonable and equitable terms in that or any other major rail system. If so, the proper solution might be to preserve them for a time as independent carriers—a solution that might well be foreclosed, once the Penn-Central merger is consummated, in view of the anticipated impact upon the three roads.

Thus, by permitting consummation of the Penn-Central merger now, the Commission may have lost two of its options for preserving the viability of the protected roads—(1) inclusion of them in an independent Norfolk and Western, (2) their temporary preservation as independent carriers. We do not argue that either solution is in fact preferable to the inclusion of the protected roads in Penn-Central or in a merged Norfolk and Western-C&O-B&O system, or that, in fact, Norfolk and Western cannot, alone, absorb the protected roads, notwithstanding their continued financial weakness and the competition that Penn-Central will give. We say only that those questions must be resolved by the Commission before the Penn-Central merger is irrevocably consummated.

CONCLUSION

In sum, we believe the Commission and the court below should not have allowed consummation of the Penn-Central merger until the fate of the smaller roads affected had been resolved. That conclusion

might suggest a remand of the case to the Commission with instructions to reopen the Penn-Central merger proceeding and consolidate it with the proceedings looking to inclusion of the smaller eastern roads in a major system and to formulation of interim protective conditions for the benefit of those roads. In the special circumstances of this case, however, such a remand may not be necessary.

We have already elaborated the view of the responsible agencies of the Executive Branch that prompt consummation of the Penn-Central merger is in the national interest if appropriate provision can be made for the other roads adversely affected. Accordingly, we believe every effort should be made, consistent with sound administrative practice, to avoid time-consuming repetitive hearings. The Penn-Central proceeding has been completed after more than four years. In August of this year, the examiner concluded the evidentiary hearings with respect to the petition for inclusion of Erie-Lackawanna, Delaware and Hudson, and Boston and Maine in the Norfolk and Western system and his report may be issued shortly. And the proceeding on interim protective conditions for the three roads, while still uncompleted, is advancing on an expedited schedule.[24] At this late date, it would be wasteful to require the Commission to begin anew. If a prompt decision is forthcom-

[24] Hearings began on October 31 and, as expressly permitted by this Court's order granting a stay, have continued in the interim. The capital indemnity question has already been submitted to the full Commission. The other matters will be submitted to the Commission on a certified record, without awaiting the usual report of the examiners.

ing, it seems preferable to await the outcome of the ongoing proceedings—which may satisfactorily resolve the problems created by the merger without the harmful delays which reopened hearings might produce.

To this end, we suggest that the Court continue its stay and hold the case for a reasonable time after the scheduled arguments to enable the Commission to correct its own error by expeditiously concluding the related proceedings. If, in the interim, the Commission resolves the fate of the smaller roads affected by the merger, the issue now presented would appear in a different light and plenary consideration here would no longer seem necessary. In that event, this Court might return the case to the district court with instructions to promptly hear, in a consolidated proceeding, any complaints filed with respect to the administrative determination. Only if the Commission is unable to promptly resolve the problems resulting from the merger would we deem it appropriate to urge this Court to reach the merits of the appeals and reverse the judgment below.

Respectfully submitted.

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RICHARD A. POSNER,
Assistants to the Solicitor General.
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NOVEMBER 1966.

APPENDIX

ORDER

At a General Session of the Interstate Commerce Commission, held at its office in Washington, D.C., on the 4th day of October, A.D. 1966.

Finance Docket No. 23832

NORFOLK AND WESTERN RAILWAY COMPANY—MERGER, ETC.—THE CHESAPEAKE AND OHIO RAILWAY COMPANY

Finance Docket No. 23833

NORFOLK AND WESTERN RAILWAY COMPANY—STOCK ISSUANCE

Upon consideration of the record in the above-entitled proceeding, including the facts, views, and arguments stated by the parties at a pre-hearing conference on September 8, 1966, before a hearing officer of this Commission; and

It appearing, That the applicants herein request the Commission, without any further delay, to set the instant proceedings for oral hearing and to specify procedures for distribution of testimony and exhibits among the parties in order to expedite the course of such hearing;

It further appearing, That the Erie-Lackawanna Railroad Company (Erie-Lackawanna), Delaware and Hudson Railroad Corporation (Delaware and Hudson), and Boston and Maine Corporation (Boston and Maine), joined by certain other parties to this proceeding, assert that commencement of hearings in the

instant merger application would deprive them of an opportunity adequately and intelligently to prepare and present their positions regarding the proposed merger, in view of other related issues now pending before the Commission in other proceedings;

It further appearing, That applicant Norfolk and Western Railway Company (Norfolk and Western), by virtue of its participation in the consummation on October 16, 1964, of the merger, control, and other transactions authorized by the Commission in Finance Docket No. 21510 (324 I.C.C. 1), affirmed its irrevocable assent to certain conditions imposed therein by the Commission, including those conditions identified in the Commission's order as Appendix O, regarding the inclusion of Erie-Lackawanna, Delaware and Hudson, and Boston and Maine in the Norfolk and Western system;

It further appearing, That the Erie-Lackawanna, Delaware and Hudson, and Boston and Maine have petitioned the Commission for inclusion in the Norfolk and Western in accordance with the provisions of the said Appendix O under terms to be determined by the Commission, and that the pending procedures to determine the matters presented by such petitions for inclusion represent the final phase of the proceedings and transactions at issue in Finance Docket No. 21510;

It further appearing, That the Erie-Lackawanna, Delaware and Hudson, and Boston and Maine are entitled to a prompt decision upon their petitions for inclusion in Norfolk and Western as contemplated by the provisions of the said Appendix O, and that such decision could materially affect the terms upon which the merger proposed herein is based;

It further appearing, That the Commission has prescribed and followed special procedures to expedite the

hearings and facilitate the prompt determination of the said petitions for inclusion, and pursuant to which special procedures the Commission to date has completed the taking of evidence and has received the opening briefs from the parties;

It further appearing, That following the issuance of an initial report by the hearing officer in the inclusion proceeding, the Commission will continue to expedite the matter; as a consequence of which the parties may expect a decision by the entire Commission within the reasonably near future;

It further appearing, That by its report and order of September 16, 1966, — I.C.C. —, in Finance Docket No. 21989 (prior report at 327 I.C.C. 475), the Commission reopened that record for a limited further hearing regarding, among other matters relevant here, a proposal for a capital loss indemnification for the Erie-Lackawanna, Delaware and Hudson, and the Boston and Maine;

It further appearing, That by an order entered September 30, 1966, in Finance Docket No. 21989, the Commission has assigned for hearing the issues of the limited further hearing in accordance with a special procedure to expedite their disposition; by which procedure the issue of capital loss indemnification (which is related to the issues in the inclusion of the Erie-Lackawanna, Delaware and Hudson, and Boston and Maine in the Norfolk and Western in Finance Docket No. 21510) can be heard first, apart from the other issues in Finance Docket No. 21989, and be certified to the Commission for initial and immediate decision, dispensing with a preliminary report by a hearing examiner;

It further appearing, That the merger application proposal advanced in Finance Docket No. 23832 pre-

sents a wide range of far-reaching, difficult and complex matters of fact and law which will require extensive hearings before an appropriate record is available to the Commission for its decision;

It further appearing, That both applicants herein, Norfolk and Western and Chesapeake and Ohio Railway Company (Chesapeake and Ohio), with the approval of the Commission under section 5(2) of the Interstate Commerce Act, have consummated other major railroad unifications within the past four years, without providing any indication that they contemplated or required any further unifications in the foreseeable future;

It further appearing, That neither Norfolk and Western nor Chesapeake and Ohio found it necessary, *during the Commission's* development of the record in Finance Docket No. 21989, to take a position adverse to the proposed merger of the Pennsylvania Railroad Company and the New York Central Railroad Company, nor to advise the Commission of any conditions necessary to protect their interests if that merger should be approved;

We find, That in view of the factors outlined above, the commencement of oral hearings in Finance Docket No. 23832 in advance of the Commission's determination of the issues involved in Finance Docket No. 21510 would preclude Erie-Lackawanna Railroad Company, Delaware and Hudson Railroad Corporation, and Boston and Maine Corporation, and other parties of record herein, from adequately preparing and presenting their positions regarding prospective effects of the merger proposed herein;

We further find, That the decision on the inclusion petitions in Finance Docket No. 21510, and the consequences thereof, could so affect the terms of the

merger proposed herein as to render premature, the commencement of the requested oral hearings at this time;

We further find, That the commencement of oral hearings in Finance Docket No. 23832 would tend to interpose new and complex factual, legal, and procedural issues into the existing situation of railroad unification in the eastern district and unduly delay the disposition thereof in Finance Docket No. 21510 and Finance Docket No. 21989;

It is ordered, That the request of applicants in Finance Docket No. 23832 for immediate commencement of the hearings thereon be, and it is hereby, denied; and that further processing of the instant applications will be held in abeyance pending further order of the Commission.

By the Commission.

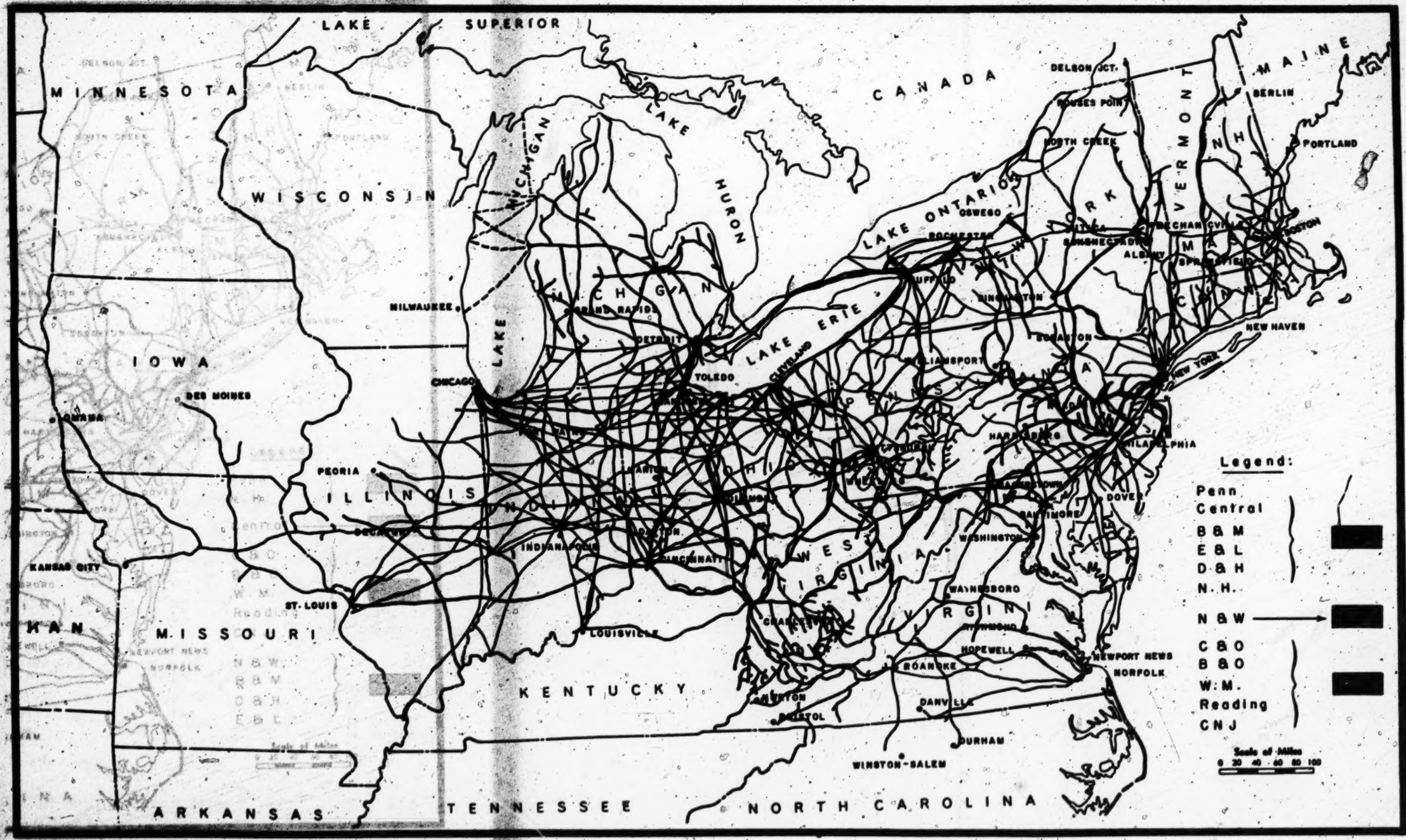
[SEAL]

H. NEIL GARSON,
Secretary.

U.S. GOVERNMENT PRINTING OFFICE: 1966

MAP NO. 1

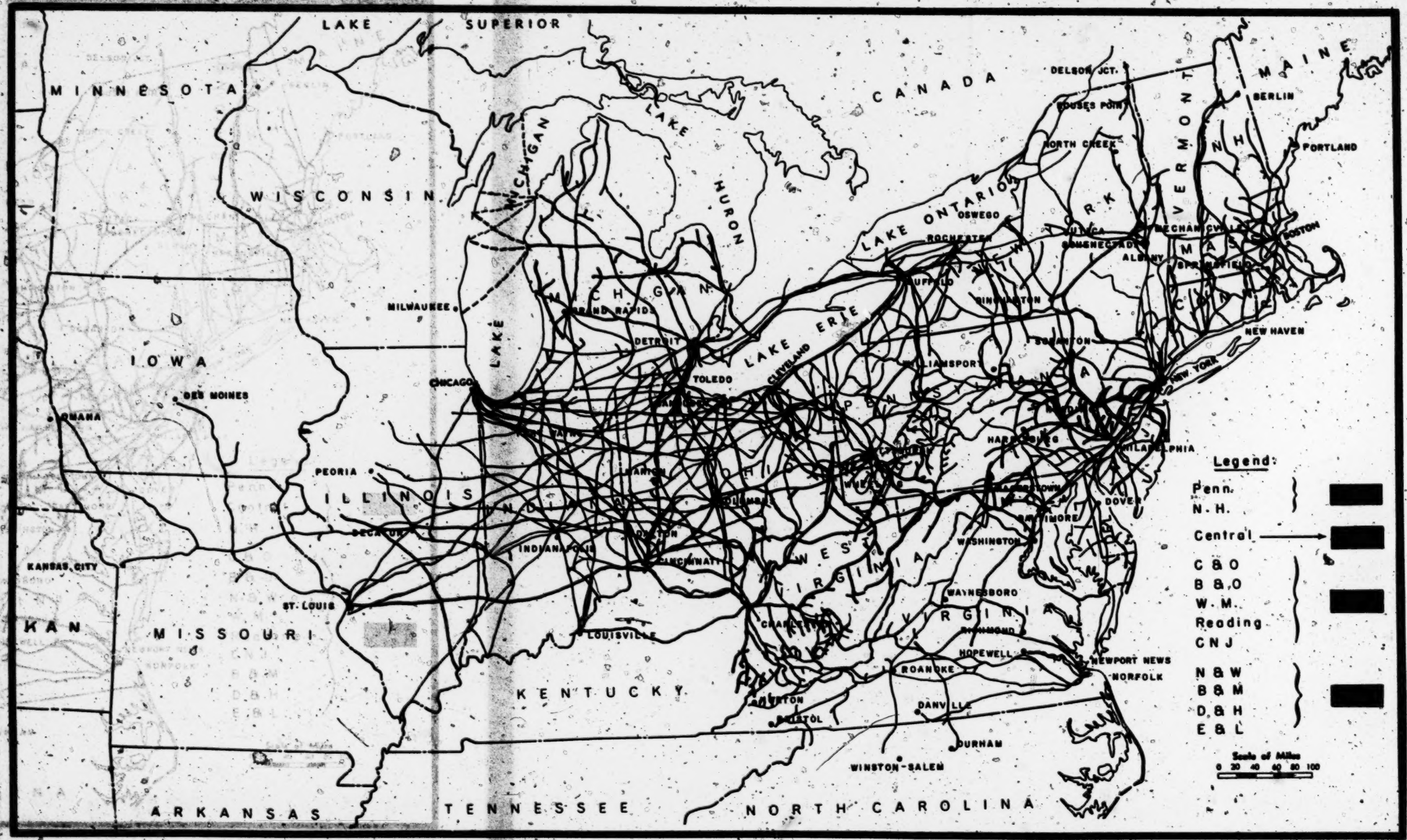
N NORFOLK & WESTERN THREE SYSTEM EASTERN DISTRICT, WITH SMALLER LINES INCLUDED IN PENN-CENTRAL



220-864 O - 68 (Face blank p. 39) No. 1

MAP NO. 2

FOUR SYSTEM EASTERN DISTRICT WITH THREE PROTECTED ROADS INCLUDED IN NORFOLK & WESTERN



MAP NO. 3

TWO SYSTEM EASTERN DISTRICT, SHOWING N&W MERGED INTO C&O-B&O